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FERC Issues “Smart Grid” Policy Statement

On July 16, 2009, the Federal Energy Regulatory Commission (FERC) issued its Policy Statement on Smart Grid Policy,¹ which provides guidance on its policies regarding development of interoperability standards for “smart grid”² devices and systems, and adopts an Interim Rate Policy for the recovery of smart grid-related costs while interoperability standards are being developed. The Policy Statement largely adopts the proposals set forth in the smart grid Proposed Policy Statement and Action Plan issued on March 19, 2009,³ and discussed in our earlier client alert.⁴ The Interim Rate Policy will become effective on September 25, 2009.

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I. Background

FERC explains that its interest in, and responsibilities regarding, smart grid development derive from (1) its authority over the rates, terms and conditions of transmission and wholesale sales in interstate commerce under Section 205 of the Federal Power Act (FPA), (2) its responsibility for approving and enforcing mandatory reliability standards for the bulk-power system in the United States under Section 219 of the FPA, and (3) its responsibilities under Section 1305 of the Energy Independence and Security Act of 2007 (EISA)⁵ to adopt smart grid interoperability standards and protocols.⁶

II. FERC Jurisdiction over Smart Grid-Related Standards

In the Policy Statement, FERC finds that, while EISA does not alter the FPA’s jurisdictional boundaries between federal and state regulation, it does give FERC a mandate to adopt smart grid-related standards. In FERC’s view, this mandate gives FERC the authority to adopt standards that will be applicable to all electric power facilities and devices with smart grid features, including those at the local distribution level and those used directly by retail customers. FERC acknowledges that EISA does not make any such standards mandatory and does not give FERC the authority to make or enforce such standards.



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III. Priorities for Smart Grid Interoperability Standards Development

In the Policy Statement, FERC adopts its proposals in the Proposed Policy Statement regarding its key standards development priorities – system security (or cybersecurity) and inter-system communication – and the four key smart grid functionalities: (1) wide-area situational awareness (i.e., the visual display of interconnection-wide system conditions in near real time at the reliability coordinator level and above), (2) demand response, (3) electric storage, and (4) electric transportation.⁷ FERC rejected proposals by commenters to adopt additional policy priorities, such as the development of standards for: existing resources or equipment and cost effective integration of legacy equipment; interfaces between utilities; and limitations on access to, and use of individual customer power usage information.

IV. Interim Rate Policy for Smart Grid Investments

As part of the Policy Statement, FERC also adopts the proposed Interim Rate Policy for recovery of the costs of smart grid investments. In order to take advantage of the Interim Rate Policy, a public utility must file either a petition for declaratory order or an FPA Section 205 rate filing demonstrating that the four criteria discussed below are satisfied. In addition, FERC will permit smart grid investments to qualify for a number of incentive rate treatments, as discussed below. Finally, FERC concludes that there is no need for special procedures for rate recovery filings for projects that also receive funding under the Department of Energy (DOE) smart grid programs. The Interim Rate Policy will remain in effect until relevant interoperability standards have been adopted through FERC rulemakings under EISA Section 1305(d).

A. Required Demonstrations

First, the applicant must demonstrate that the smart grid facilities will advance the goals of EISA Section 1301. To make this threshold showing, the applicant must describe the proposed investment (including the technologies, systems, and applications it entails) and how it is consistent with the policy and one or more of the goals Congress set forth in Section 1301 of EISA.⁸

Second, an applicant must show that the reliability and security of the bulk-power system will not be adversely affected by the smart grid facilities at issue. The applicant would have to show how it will maintain compliance with these standards during and after the installation of smart grid technologies. In addition, the applicant must address: (1) the integrity of data communicated; (2) the authentication of the communications; (3) the prevention of unauthorized modifications to smart grid devices and the logging of all modifications made; (4) the physical protection of smart grid devices; and (5) the potential impact of unauthorized use of these smart grid devices on the bulk-power system.

Third, the applicant must demonstrate that it has minimized the possibility of stranded investment. To do so, the applicant must show that it has relied to the greatest extent practical on existing, widely adopted and open interoperability standards, and that, where feasible, it has relied on systems and firmware that can be securely upgraded readily and quickly.



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Finally, the applicant must agree to share information concerning the applicable smart grid facilities with the DOE Smart Grid Clearinghouse.

B. Incentive Rate Treatment

FERC adopts its proposal to permit the following incentive rate treatments. First, FERC will permit single-issue rate treatment for such investments, so that public utilities will be able to recover the costs of these investments without opening their entire rate base to FERC review. Second, FERC will permit applicants to seek recovery of otherwise stranded costs of legacy systems that are to be replaced by smart grid equipment. Finally, FERC will accept requests for incentive rate treatments such as accelerated depreciation and abandonment authority (whereby an applicant is assured of recovery of abandoned plant costs if the project is abandoned for reasons outside the control of the public utility) specifically tied to smart grid deployments under FERC's FPA Section 205 authority.

¹ *Smart Grid Policy*, 128 FERC ¶ 61,060 (2009) (Policy Statement).

² According to FERC, smart grid development involves the application of digital technologies to the grid to enable real-time coordination of information from generation supply resources, demand resources, and distributed energy resources, which will bring new efficiencies to the electric system through improved communication and coordination between utilities and with the grid, translating into savings in the provision of electric service. The smart grid concept envisions a power system architecture that permits two-way communication between the grid and essentially all devices that connect to it, ultimately all the way down to large consumer appliances, which will be able to respond automatically to customer-selected price or dispatch signals delivered over the smart grid infrastructure.

³ *Smart Grid Policy*, 126 FERC ¶ 126 FERC 61,253 (2009) (Proposed Policy Statement).

⁴ [King & Spalding Client Alert on Proposed Policy Statement](#)

⁵ Pub. L. No. 110-140, 121 Stat. 1492 (2007).

⁶ Section 1305(a) of EISA directs the National Institute of Standards and Technology (NIST) to coordinate the development of a "framework that includes protocols and model standards to achieve the interoperability of smart grid devices and systems." EISA § 1305(a) (*to be codified at* 15 U.S.C. § 17385(a)). Section 1305(d) provides that, once FERC is satisfied that NIST's work on particular protocols or standards has led to "sufficient consensus," FERC is to "institute a rulemaking proceeding to adopt such standards and protocols as may be necessary to insure smart-grid functionality and interoperability in interstate transmission of electric power, and regional and wholesale electricity markets." EISA § 1305(d) (*to be codified at* 15 U.S.C. § 17385(d)).

⁷ For a more detailed discussion of the proposed standards and functionalities, [click here](#).

⁸ These goals include increased use of digital information and controls technology to improve reliability, security, and efficiency of the electric grid, dynamic optimization of grid operations and resources, with full cybersecurity, and deployment and integration of distributed resources and generation, including renewable resources, demand side resources and energy efficiency resources. EISA § 1301 (*to be codified at* 15 U.S.C. § 17381).

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